

Issues regarding the taxation of software and software licenses may be found at 86 Ill. Adm. Code 130.1935. (This is a GIL.)

April 24, 2006

Dear Xxxxx:

This letter is in response to your letter dated February 13, 2006, in which you request information. The Department issues two types of letter rulings. Private Letter Rulings ("PLRs") are issued by the Department in response to specific taxpayer inquiries concerning the application of a tax statute or rule to a particular fact situation. A PLR is binding on the Department, but only as to the taxpayer who is the subject of the request for ruling and only to the extent the facts recited in the PLR are correct and complete. Persons seeking PLRs must comply with the procedures for PLRs found in the Department's regulations at 2 Ill. Adm. Code 1200.110. The purpose of a General Information Letter ("GIL") is to direct taxpayers to Department regulations or other sources of information regarding the topic about which they have inquired. A GIL is not a statement of Department policy and is not binding on the Department. See 2 Ill. Adm. Code 1200.120. You may access our website at www.tax.illinois.gov to review regulations, letter rulings and other types of information relevant to your inquiry.

The nature of your inquiry and the information you have provided require that we respond with a GIL. In your letter you have stated and made inquiry as follows:

ABC is registered to collect sales tax in your state. We are a software developer and retailer. We have some items that we will be invoicing to our customers located in your state and we need to know if these items are taxable per your regulations.

The first item is software maintenance agreement. Is this item taxable in your state? Also does the delivery of the update that goes out once a year affect the taxability of the software maintenance? Please see the enclosed document for a description of this service.

The second item is a recurring license fee. Our customer is still licensing our software but instead of paying us up front for a license, they will pay us over time, or in some cases, may pay upfront for a specific period of time. Another way of putting it is that they are paying us monthly for a license to use our software. No title to or ownership of the ABC software or any part thereof is transferred to the customer.

The third item is hosting fee. This is an optional service. The computer is located at another location, the state of STATE. The customer accesses their software on the shared computer, like time sharing on a computer. The purchaser of the software license is not required to purchase the hosting service. Please see the enclosed documents for a description of this service.

Also, we need to know if the following our taxable in your state:

- Programming - making modifications/enhancements to the already purchased canned software. This is separately billed from the software purchase.
- Consulting - study of information management. We are not consulting on the core of business. This is separately billed from the software purchase.
- Training - help on how to use the software system. This training can be held at our office in CITY/STATE or an employee of ABC may travel to the customer's location.
- Training over the web - help on how to use the software system by working with the customer over the intranet.
- Implementation - installation or setup of a computer system or software.
- Transactions - our transactions are completely internet based. These transactions are processed over the internet to any location. There is no tangible personal property received by the customer. (Please see enclosed brochure.)
- Fixed fees - is for a mailbox where the transaction's are sent, here they are dispersed and sent to the locations directed. In turn the location can send back a received notice. Again, this is all internet based. There is no tangible personal property received by the customer. (Please see enclosed brochure.)
- Billable support - assistance via phone/internet that is not included in the maintenance agreement.

I have emailed this letter to the department of revenue but I am only getting general answers in response. For ABC to be taxing per your states regulations we need direct answers to our questions of taxability. We also would like to know the exact regulations that each of these items fall under.

We would appreciate your prompt response to this inquiry so that we will be proceeding in accordance to your states [sic] regulations.

DEPARTMENT'S RESPONSE:

General information letters are used to direct taxpayers to the Department's regulations and other sources of information for general guidance. You may find the Department's general information letters helpful in regards to many of the issues raised in your request. The Department's "Sunshine Letter" rulings are located on the Department's Internet website under the heading of "Laws/Regs/Rulings." Issues regarding the taxation of software and software licenses may be found at 86 Ill. Adm. Code 130.1935.

In general, maintenance agreements that cover computer software and hardware are treated the same as maintenance agreements for other types of tangible personal property. Please refer to 86 Ill. Adm. Code Sec. 130.1935(b). The taxability of maintenance agreements depends upon if charges for the agreements are included in the selling price of the tangible personal property. If the charges for the agreements are included in the selling price of the tangible personal property, those charges are part of the gross receipts of the retail transaction and are subject to tax. No tax is incurred on the maintenance services or parts when the repair or servicing is performed.

If maintenance agreements are sold separately from tangible personal property, sales of the agreements are not taxable transactions. However, when maintenance services or parts are provided under the maintenance agreements, the service or repair companies will be acting as

service providers under provisions of the Service Occupation Tax Act that provide that when service providers enter into agreements to provide maintenance services for particular pieces of equipment for stated periods of time at predetermined fees, the service providers incur Use Tax based on their cost price of tangible personal property transferred to customers incident to the completion of the maintenance service. See 86 Ill. Adm. Code Sec. 140.301(b)(3).

Generally, sales of “canned” computer software are taxable retail sales in Illinois. Sales of canned software are taxable regardless of the means of delivery. For instance, the transfer or sale of canned computer software downloaded electronically would be taxable. However, if the computer software consists of custom computer programs, then the sales of such software may not be taxable retail sales. See 86 Ill. Adm. Code 130.1935(c). Custom computer programs or software must be prepared to the special order of the customer.

Charges for updates of canned software are fully taxable pursuant to Section 130.1935. If the updates qualify as custom software under Section 130.1935(c), they may not be taxable. But, if maintenance agreements provide for updates of canned software, and the charges for those updates are not separately stated and taxed, then the whole agreements would be taxable as sales of canned software.

I hope this information is helpful. If you require additional information, please visit our website at www.tax.illinois.gov or contact the Department’s Taxpayer Information Division at (217) 782-3336. If you are not under audit and you wish to obtain a binding PLR regarding your factual situation, please submit a request conforming to the requirements of 2 Ill. Adm. Code 1200.110 (b).

Very truly yours,

Edwin E. Boggess
Associate Counsel

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